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STATE OF SOUTH CAROLINA
State Budget and Control Board
DIVISION OF INSURANCE AND GRANTS SERVICES

JIM HODGES, CHAIRMAN
GOVERNOR
GRADY L. PATTERSON, JR.
STATE TREASURER
JAMES A. LANDER
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John Clark
Director

November 27, 2002

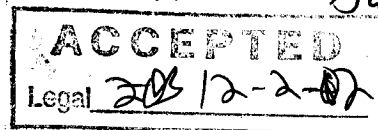
Mr. Gary Walsh, Executive Director
South Carolina Public Service Commission
P. O. Drawer 11649
Columbia, S.C. 29210

Dear Mr. Walsh:

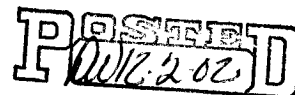
Staff of the State Budget and Control Board and Chem-Nuclear Systems, LLC, have been meeting to discuss the Operations and Efficiency Plan that was ordered by the PSC. Mutual concerns include how the information, data, and issues addressed in the report might best be applied to the Commission's allowable cost proceedings.

These discussions have resulted in the attached joint statement for consideration of the Commission. Both parties to this statement stipulate and agree that they will not present, offer, or rely upon the OEP Study as relates to this application. Further, they will not present testimony or evidence relating to the OEP Study. Both parties believe that it would not be productive to attempt to defend or to challenge the detailed information in this 300 page report as part of the forthcoming hearings on Chem-Nuclear's allowable cost application for fiscal year 2003. This is due to the complexity of the report and because the application for fiscal year 2003 has already been submitted.

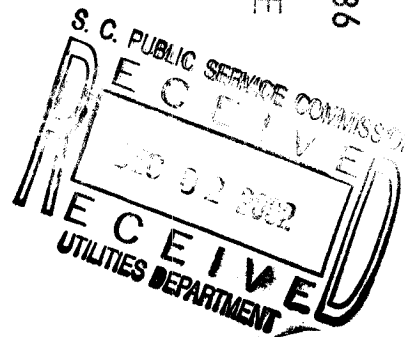
Both parties have agreed to a framework that should lead to a recommendation to the Commission on how the information in the report may be relevant to subsequent allowable cost proceedings. It is our intention to resolve as many of these issues as possible before subsequent hearings. At a minimum, we expect to clarify any differences and narrow the issues that will be necessary for the Commission to consider.



HUGH K. LEATHERMAN, SR.
CHAIRMAN, SENATE FINANCE COMMITTEE
ROBERT W. HARRELL, JR.
CHAIRMAN, WAYS AND MEANS COMMITTEE
FRANK W. FUSCO
EXECUTIVE DIRECTOR

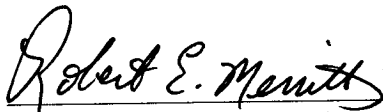


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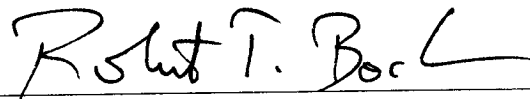


In addition, our discussions have resulted in progress on certain other issues. In particular, we believe we are close to agreement on the details of a proposed employee retention compensation plan. We are discussing changes to the initial plan that will better link the incentives for CNS with our State objective of optimizing revenues for education. We are hopeful that the final agreement will be one that the Commission and its staff can also support.

We respectfully submit the enclosed joint statement that provides background on the study and our recommendations on how the Commission might proceed.



Robert E. Merritt, Esq., Attorney for the
State Budget and Control Board



Robert T. Bockman, Esq., McNair Firm,
Attorney for Chem-Nuclear, LLC

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John Clark
Director

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MEMORANDUM

TO: Parties of Record – Public Service Commission Docket #2000-366-A –
Application of Chem-Nuclear Systems, LLC, A division of Duratec, Inc., for adjustment in the levels of
allowable costs and for identification of allowable costs.

FROM:  Robert E. Merritt, Esq., Attorney for the Budget and Control Board

SUBJ: Joint Statement for Consideration of PSC

Staffs of the Budget and Control Board, the Public Service Commission, and Chem-Nuclear Systems (CNS), LLC, have been meeting to discuss the Operations and Efficiency Plan developed in response to the PSC Order No. 2001-499. Mutual concerns include how the information, data, and issues addressed in the report might best be applied to the Commission's allowable cost proceedings.

These discussions have resulted in a joint statement for consideration of the Commission. Both parties to this statement stipulate and agree that they will not present, offer, or rely upon the OEP Study as relates to this application. Further, they will not present testimony or evidence relating to the OEP Study. Both parties believe that it would not be productive to attempt to defend or to challenge the detailed information in this 300 page report as part of the upcoming hearings on Chem-Nuclear's allowable cost application for fiscal year 2003. This is due to the complexity of the report and because the application for fiscal year 2003 has already been submitted.

Both parties have agreed to a framework that should lead to a recommendation to the Commission on how the information in the report may be relevant to subsequent allowable cost proceedings. It is our intention to resolve as many of these issues as possible before any subsequent hearing. At a minimum, we expect to clarify any differences and narrow the issues that will be necessary for the Commission to consider.

Attached is a joint statement of the Budget and Control Board and CNS that provides background on the study and recommendations on how the Commission might proceed. We would respectfully request your review and support of the recommendations. If you have any questions as to the statement and recommendations or would like to participate in any future discussions, please call Bill Newberry at 803-737-8037.

cc: Gary Walsh
David Butler, Esq.

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Joint Statement and Proposal
Chem-Nuclear Systems, LLC
South Carolina Budget and Control Board

This statement pertaining to the "Application of Chem-Nuclear Systems, LLC for Adjustment in the Levels of Allowable Costs and for Identification of Allowable Costs for Fiscal Year 2002-2003" (Docket No. 2000-366A) is jointly submitted by Chem-Nuclear Systems, LLC, the applicant, and the South Carolina Budget and Control Board, a party to the docket (together referred to herein as "the parties").

In its Order of June 1, 2001 (Order No. 2001-499), the Commission expressed its awareness that some costs of operating the Barnwell low-level radioactive waste disposal facility were "fixed" and some were "variable." Fixed costs are those that do not change in response to changes in waste volumes and other measures, while variable costs do increase or decrease in direct or indirect relationship to some discrete measure of business activity. One significant measure of business activity is the volume of waste received, and that volume is expected to decline significantly at least through the year 2008.¹ Because of conflicting testimony leading up to the Order, the Commission conceded that it was not able to identify with precision exactly which operating costs were fixed and which were variable.

As a result, the Order prescribed a relatively simple formula under which costs for concrete disposal vaults and amortization of the construction costs for waste trenches would be considered the only variable costs. All other costs would be considered fixed costs, regardless of the volume of waste accepted or other variables that might affect the level of business activity. The two applications for allowable costs that Chem-Nuclear has filed since the June 2001 Order have reflected the prescribed formula for fixed and variable costs.

While Chem-Nuclear's applications for allowable costs since then have reflected the prescribed formula for fixed and variable costs, the Commission also initiated a strategy that might lead to better quantification of fixed and variable costs as waste volumes are ramped down in the coming years. The June 2001 Order states:

"In any event, we do believe that reductions in fixed and variable costs should result from reductions in the waste stream to the Chem-Nuclear facility. This conclusion is consistent with the testimony of Dr. Robert A. Fjeld. To quantify these future cost reductions, Chem-Nuclear shall provide to the Commission an operations and efficiency plan for the Barnwell facility prepared by an independent qualified party... The plan shall be completed prior to June 30, 2002..." (page 29)

¹ South Carolina State law at 48-46-40(A)(6)(a) specifies a sharp ramp-down in the volume of waste that can be accepted at the Barnwell site through year 2008. After that date, the site may only accept waste generated in the Atlantic Compact, which consists of South Carolina, Connecticut and New Jersey.

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The Operations and Efficiency Plan (OEP) that was prepared in response to the Commission's Order may provide a basis to better identify specifically which operating costs are fixed and which vary with respect to some measure of business activity.

The current practice for awarding allowable costs entails the annual submission by Chem-Nuclear of an application for allowable costs for the fiscal year in which the application is filed. The application lists "fixed" cost accounts (budget line items), provides the amount of money awarded by the Commission for each cost account in the previous year's proceedings, and provides the actual dollars spent in each account during the year. In cost account lines where the actual expenditure is less than the approved amount, Chem-Nuclear forfeits the difference and recovers only the actual amount spent. For cost account lines where the actual expenditure exceeds the amount previously awarded, Chem-Nuclear requests reimbursement for the difference, in accordance with 48-46-40(B)(4), S.C.Code. In addition, the application provides actual dollar values to serve as adjustment to the amounts awarded as variable costs for concrete disposal vaults and trench amortization. This portion of the application is essentially a true-up proceeding.

Another part of the application includes a requested dollar amount for each cost account for the year in which the application is submitted. Once approved, the requested amount serves as the allowable cost basis for the fiscal year until the Commission's true-up proceeding in the following year.

Should this method of awarding allowable operating costs continue, then the identification of which components of work, as identified in a detailed work breakdown structure (WBS), are fixed and which are variable would not serve a regulatory purpose. The cost in each cost category in Chem-Nuclear's chart of accounts is what it is. Clearly, these "fixed costs" are not absolutely fixed because virtually each cost category differs by some amount from year to year. In addition, fixed cost categories are sometimes imbued with "irregular" costs, ad hoc costs that result from episodic costs associated with operational or regulatory requirements that cannot be predicted from year to year.

The question the parties face is how to apply the information and data in the OEP in a manner that furthers the Commission's regulatory responsibilities under South Carolina law. The parties believe that the OEP could yield useful information and data that might be applied in some direct fashion in subsequent proceedings on allowable costs. The parties believe that a more detailed understanding of the variables associated with operating costs could provide the Commission with information that could lead to a refined formula for fixed and variable costs.

The parties agree that the detailed WBS in the OEP can serve as the basis for better identifying fixed, variable, and irregular costs. The parties have held preliminary discussions to address: (1) the categorization of certain elements of the WBS as either fixed, variable or irregular, (2) the unit costs assigned to each of the elements of the WBS, and (3) the number of units, generally expressed in hours of labor, assumed for each element of the WBS, and (4) the labor rates or other rates applied to each of the

elements. The parties do not necessarily agree at this point on the categorization, units' costs, number of units or labor rates that are presented in the OEP.

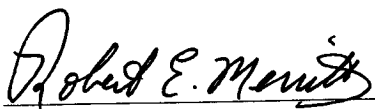
The parties believe that further discussions and analysis might result in mutual agreement on the issues set forth above. Ideally, agreement on which costs are fixed and which are variable, and the level of costs associated with each, could result in a formula that could be used as the basis for awarding allowable costs to Chem-Nuclear without the need to re-approve each cost element each year. Under this approach, costs would be divided into three distinct categories; Fixed costs, Variable costs, and Irregular costs.

At worst, continued discussions among the parties will result in clearer identification of specific technical areas where the parties agree and where they disagree. The parties believe that technical discussions of this type are a productive and efficient way to arrive at resolution to the question of fixed, variable and irregular costs. Until there is better identification and definition of these cost issues, the parties believe that examination of these issues in the upcoming hearings related to allowable costs for fiscal year 2003 would be confusing, expensive, contentious and unproductive. Should the parties arrive at a recommendation related to fixed, variable and irregular costs, that entails changes to the method prescribed for applying for allowable costs, such a change would not be applicable prior to fiscal year 2004, since the statutory deadline for applying for 2003 allowable costs has already past.

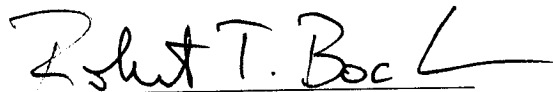
Because of this, the parties jointly recommend that:

- These proceedings held pursuant to PSC Order No. 2001-499 related to fiscal year 2003 allowable costs and adjustments for fiscal year 2002 continue as scheduled;
- These proceedings not include consideration or examination of the content of the OEP and application or relevance of the study to allowable costs in fiscal year 2002 or 2003; and
- The Commission encourage the parties, in consultation with the PSC staff, to continue to meet through the fiscal year to evaluate the OEP and other information and data related to fixed and variable costs. Based on these discussions, the Commission late in this fiscal year may consider a proposal from one or both of the parties for changing the method of awarding fixed and variable allowable costs for use in fiscal year 2004 and beyond.

Respectfully submitted,



Robert E. Merritt, Esq., Attorney for
State Budget and Control Board



Robert T. Bockman, McNair Firm,
Attorney for Chem-Nuclear, LLC